In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 1352

FRANCIS T. NORMAN AND MARGUERITE M. NORMAN, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR RESPONDENT IN OPPOSITION

Taxpayer and his wife (petitioners) did not report on their joint federal income tax returns for the years 1958 through 1962 various monies taxpayer had secretly misappropriated or embezzled from his employer during those years. After the employer discovered the shortages in October 1962, taxpayer made repayment in full pursuant to a settlement agreement (Pet. 14–17, 22–25). On these facts, the Tax Court rejected petitioners' contention that the 1962 agreement required that the defalcations be treated as loans for tax purposes. It held (Pet. 26–29) that the misappropriated funds were taxable income to petitioners in the years received, but that, as the Commissioner had conceded, the repayment gave rise

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to a deductible loss for the taxable year 1962 under 26 U.S.C. 165(c)(2). The court of appeals affirmed (Pet. 10–14).

1. In *James* v. *United States*, 366 U.S. 213, this Court held that funds obtained through embezzlement constitute taxable income in the year acquired, even though, as in the case of gains received by mistake, there may be a yet unrecognized obligation to repay. Any repayment gives rise to a deduction in the year in which it is made.

The plurality opinion in *James* (which attracted six votes on this point) distinguishes loans from both embezzled funds and gains received by mistake by noting that the latter are received "without the consensual recognition * * * of an obligation to repay" (*id.* at 219)—*i.e.*, *bona fide* loans by their nature are accompanied when made by such consensual recognition. Petitioners contend (Pet. 6–8), in effect, that when taxpayer in 1962 agreed to make restitution, this was the kind of "consensual recognition" meant by this Court in *James*—that a later agreement for repayment can somehow relate back and transform embezzled gains into loans. As the courts below correctly concluded, this contention involves a misreading of *James* and an attempt to apply certain language taken out of context to circumstances to which it was plainly never directed.

2. The other contention made (Pet. 8) is that taxpayer's wife would be denied due process if her separate estate is subjected to the additional taxes and five percent negligence penalties involved. This contention was not presented in the court of appeals and

no special circumstances exist which would justify this Court's consideration of the question for the first time. In any event, the contention is without substance. It is well settled that, where joint returns are filed, the wife is equally liable with her husband for both the tax deficiency and any additions to tax—*e.g.*, for a fraud penalty—even though only the husband was at fault. See, *e.g.*, *Moore* v. *United States*, 360 F. 2d 353, 357 (C.A. 4), and cases there cited.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.
JOHNNIE M. WALTERS,
Assistant Attorney General.
JOSEPH M. HOWARD,
JOHN M. BRANT,
Attorneys.

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